



STATE OF WASHINGTON

OFFICE OF THE FORECAST COUNCIL

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June 3, 2003

**TO:** Governor's Council of Economic Advisors

**FROM:** Chang Mook Sohn, Executive Director  
Office of the Forecast Council

**SUBJECT: PRELIMINARY MAY ECONOMIC FORECAST**

This preliminary forecast was based on Global Insight's May Control forecast for the U.S. economy. You should have received a summary of the Global Insight forecast by email. If not, please contact our office. The forecast incorporated the advance GDP estimate for the first quarter of 2003. According to the advance estimate, real GDP grew at a 1.6 percent rate in the first quarter of 2003 following a 1.4 percent rate in the fourth quarter of 2002. With the economy growing well below its potential, employers have cut more than half a million jobs in the last three months. The most important question for the U.S. economy is whether the recent weakness is a temporary phenomenon related to war uncertainties or whether it is the result of more fundamental problems. Though consumer confidence and the stock market have improved since the war's end, it is still too early to see an impact on the broader economy. While the current U.S. forecast assumes a pick up in growth in the second half of the year, the recovery in employment and income is later and weaker than assumed three months ago.

A comparison of the preliminary U.S. forecast with the forecast adopted in March is shown in Table 2.

The aerospace forecast for Washington reflects the fact that recent declines have been more severe than expected in February as well as recently issued layoff notices resulting in a reduction of 3,600 by the fourth quarter of 2003 compared to the previous forecast. As in February, the forecast expects an additional 2,600 decline during 2004. The software wage assumption is slightly higher than in the previous forecast due to an improvement in the outlook for Microsoft stock option income. The forecast still assumes there will be no major fluctuations in Microsoft stock option activity in the future. In 2002 we saw the first ever year-over-year decline in software employment. The forecast assumes a resumption of positive growth of about 350 per quarter, accelerating to 650 per quarter by the end of the year.

This forecast also incorporates newly available Covered Employment and Payrolls (ES-202) data for the fourth quarter of 2002. The revision to employment subtracted 9,200 from the level of employment in December. Employment growth since December has also been weaker than assumed in February, leaving the April level 20,100 lower than expected. The ES-202 data also indicate that fourth quarter wages were \$0.458 billion lower than expected in February. The software wage estimate was very close but non-software wages were \$0.482 billion lower than expected. Nonwage personal income was \$0.085 billion lower than expected in February resulting in a revision to total personal income of a negative \$0.543 billion. The forecast also reflects Seattle consumer price data for the first four months of the year, which shows local inflation running well below the national average and well below the previous forecast. Washington housing activity for the first four months of the year remains very strong, however. The May preliminary forecast for Washington reflects the recent weakness in employment, income, and prices in Washington as well as the impact of the delayed and weaker national recovery.

A comparison of the preliminary Washington forecast with the forecast adopted in March is shown in Table 3.

Review of the forecast by the Governor's Council of Economic Advisors is scheduled for Friday June 6, 2003 at 10:00 a.m., in the **Insurance Building 4<sup>th</sup> floor conference room**.

If you have any questions, please contact Bret Bertolin, Senior Economic Forecaster, at (360) 570-6106.

**PLEASE NOTE:**

Enclosed is a worksheet summarizing the preliminary forecast. **Council members are strongly encouraged to complete and return this worksheet either in person at the Governor's Council meeting or, if unable to attend, by FAX to (360) 753-7022.** This worksheet is relied on by the Forecast Council members and staff to gauge the reasonableness of the preliminary economic forecast and also serves as the basis of an alternative economic and revenue forecast.

Fluctuations in software wages due to stock option income have, in the past, caused significant distortions in overall wage and personal income trends. Except for the second quarter of 2003, these distortions are expected to be small as shown in the table below.

	2003:2	2003	2004	2005:1,2
<u>Washington Real Personal Income, %Ch.</u>				
Baseline	3.6	1.3	2.5	2.9
Excluding Software	1.3	1.5	2.3	2.8
Software's Impact	2.2	-0.2	0.2	0.1
<u>Washington Average Annual Wage, %Ch.</u>				
Baseline	7.4	2.6	2.8	3.0
Excluding Software	3.0	3.1	2.5	2.9
Software's Impact	4.2	-0.4	0.3	0.1

CMS: dym/bb  
Enclosures

Table 1  
**U.S. Economic Forecast Comparison**  
May 2003

	2003:1	2003:2	2003:3	2003:4	2002	2003	2004	2005
<b>Real GDP, Percent Change</b>								
Global Insight	1.6	1.6	4.0	4.2	2.4	2.3	4.2	3.3
Blue Chip	1.6	2.1	3.5	3.7		2.3	3.6	
Economy.com	1.6	1.7	3.6	4.1	2.4	2.3		
S&P	1.6	2.2	4.2	4.1	2.5	2.4	4.4	3.5
Merril Lynch	1.6	1.8	3.0	2.5	2.4	2.1	3.3	
<b>Federal Funds Rate</b>								
Global Insight	1.25	1.25	1.25	1.31	1.67	1.27	1.69	2.00
Blue Chip*	1.3	1.3	1.3	1.5		1.3	2.6	
Economy.com	1.25	1.25	1.25	1.29	1.67	1.26		
S&P	1.3	1.2	1.0	1.0	1.7	1.1	1.7	3.3
Merril Lynch	1.26	1.25	0.85	0.75	1.65	1.05	0.90	
<b>Consumer Price Index, Percent Change</b>								
Global Insight	3.9	1.8	0.9	1.6	1.6	2.4	1.5	1.8
Blue Chip*	3.8	1.7	1.7	1.9		2.5	2.1	
Economy.com	3.9	2.2	1.2	1.9	1.6	2.5		
S&P	3.9	1.8	0.9	1.7	1.6	2.4	1.6	2.0
Merril Lynch	3.9	-0.4	0.8	1.4	1.6	1.9	1.2	
<b>Payroll Employment, Millions</b>								
Global Insight	130.6	130.4	130.6	131.1	130.8	130.7	133.0	135.4
Economy.com	130.6	130.6	130.7	131.0	130.8	130.7		
S&P	130.6	130.5	130.7	131.1	130.8	130.7	133.1	135.9
<b>Unemployment Rate, Percent</b>								
Global Insight	5.77	6.11	6.18	6.13	5.78	6.05	5.88	5.73
Blue Chip	5.8	6.0	6.0	5.9		5.9	5.7	
Economy.com	5.8	6.0	6.2	6.2	5.8	6.0		
S&P	5.8	6.1	6.2	6.2	5.8	6.0	5.9	5.6
Merril Lynch	5.8	6.0	6.3	6.3	5.8	6.1	6.0	
<b>Real Disposable Person Income, Percent Change</b>								
Global Insight	1.1	1.6	4.6	4.6	4.3	2.3	4.3	2.5
Blue Chip	1.1	2.5	4.5	3.4		2.5	3.5	
Merril Lynch	1.1	3.1	3.9	4.0	4.3	2.5	4.1	

\* Estimate based on T-bill rate.

Table 2

**U.S. Forecast Comparison**

	2002:3	2002:4	2003:1	2003:2	2003:3	2003:4	2001	2002	2003	2004	2005
<b>Real GDP (Billions of Chained 1996 Dollars)</b>											
May	9485.6	9518.2	9556.0	9594.8	9690.3	9790.3	9214.5	9439.9	9657.8	10060.7	10390.0
Percent Change	4.0	1.4	1.6	1.6	4.0	4.2	0.3	2.4	2.3	4.2	3.3
February	9485.6	9503.2	9574.1	9651.4	9766.1	9892.8	9214.5	9436.1	9721.1	10164.7	10553.1
Percent Change	4.0	0.7	3.0	3.3	4.8	5.3	0.3	2.4	3.0	4.6	3.8
<b>Implicit Price Deflator (1996=1.000)</b>											
May	1.114	1.119	1.126	1.130	1.132	1.137	1.096	1.111	1.131	1.149	1.170
Percent Change	1.7	1.8	2.8	1.4	0.7	1.6	2.0	1.4	1.9	1.6	1.8
February	1.114	1.119	1.126	1.132	1.135	1.139	1.096	1.111	1.133	1.153	1.175
Percent Change	1.7	1.9	2.4	2.4	0.9	1.5	2.0	1.4	2.0	1.7	2.0
<b>Real Personal Income (Billions of Chained 1996 Dollars)</b>											
May	8045.0	8081.4	8102.8	8142.0	8195.4	8261.3	7927.3	8039.5	8175.4	8440.4	8695.4
Percent Change	0.3	1.8	1.1	1.9	2.6	3.3	1.3	1.4	1.7	3.2	3.0
February	8075.9	8116.5	8167.5	8210.9	8303.8	8389.3	7927.3	8056.0	8267.9	8612.3	8921.3
Percent Change	1.9	2.0	2.5	2.1	4.6	4.2	1.3	1.6	2.6	4.2	3.6
<b>Wage and Salary Employment</b>											
May	130.84	130.80	130.60	130.41	130.62	131.11	131.93	130.78	130.68	132.99	135.38
Percent Change	0.4	-0.1	-0.6	-0.6	0.6	1.5	0.2	-0.9	-0.1	1.8	1.8
February	130.84	130.81	130.75	130.91	131.32	132.11	131.93	130.78	131.27	134.34	137.26
Percent Change	0.4	-0.1	-0.2	0.5	1.3	2.4	0.2	-0.9	0.4	2.3	2.2
<b>Unemployment Rate</b>											
May	5.77	5.90	5.77	6.11	6.18	6.13	4.77	5.78	6.05	5.88	5.73
February	5.73	5.90	6.10	6.30	6.20	5.70	4.79	5.78	6.08	5.27	4.99
<b>Mortgage Rate</b>											
May	6.29	6.08	5.83	5.81	5.91	6.12	6.97	6.54	5.92	6.47	6.86
February	6.29	6.08	5.95	6.02	6.27	6.67	6.97	6.54	6.23	7.30	7.85
<b>3 Month T-Bill Rate</b>											
May	1.65	1.35	1.16	1.14	1.15	1.24	3.43	1.61	1.17	1.60	1.88
February	1.65	1.35	1.15	1.23	1.50	2.17	3.43	1.61	1.51	3.08	3.86

Table 3

**Washington Forecast Comparison**

	2002:3	2002:4	2003:1	2003:2	2003:3	2003:4	2001	2002	2003	2004	2005
<b>Real Personal Income (Billions of Chained 1996 Dollars)</b>											
May	179.271	178.610	178.696	180.278	181.269	182.319	174.919	178.354	180.641	185.207	190.151
Percent Change	1.9	-1.5	0.2	3.6	2.2	2.3	0.5	2.0	1.3	2.5	2.7
February	179.727	179.045	180.622	181.407	183.132	184.606	175.028	178.704	182.442	188.547	194.413
Percent Change	3.4	-1.5	3.6	1.8	3.9	3.3	0.6	2.1	2.1	3.3	3.1
<b>Personal Income</b>											
May	199.636	199.799	201.293	203.782	205.250	207.239	191.644	198.087	204.391	212.809	222.530
Percent Change	3.7	0.3	3.0	5.0	2.9	3.9	2.6	3.4	3.2	4.1	4.6
February	200.143	200.342	203.305	205.421	207.822	210.265	191.763	198.490	206.703	217.345	228.508
Percent Change	5.2	0.4	6.0	4.2	4.8	4.8	2.6	3.5	4.1	5.1	5.1
<b>Wage and Salary Employment</b>											
May	2662.5	2654.3	2651.2	2642.0	2645.1	2651.9	2696.3	2654.8	2647.6	2683.7	2736.8
Percent Change	1.5	-1.2	-0.5	-1.4	0.5	1.0	-0.6	-1.5	-0.3	1.4	2.0
February	2659.5	2656.7	2661.5	2664.6	2672.7	2685.2	2696.4	2654.2	2671.0	2729.7	2793.8
Percent Change	1.1	-0.4	0.7	0.5	1.2	1.9	-0.6	-1.6	0.6	2.2	2.3
<b>Manufacturing Employment</b>											
May	308.5	301.0	298.1	294.2	290.0	287.7	338.3	309.9	292.5	287.2	292.3
Percent Change	-4.3	-9.4	-3.7	-5.2	-5.6	-3.1	-4.2	-8.4	-5.6	-1.8	1.8
February	308.4	302.1	299.2	296.0	292.9	291.5	338.3	310.1	294.9	292.3	296.6
Percent Change	-4.6	-8.0	-3.8	-4.2	-4.1	-1.9	-4.2	-8.3	-4.9	-0.9	1.5
<b>Construction Employment</b>											
May	153.1	153.6	153.8	153.8	154.7	154.2	155.4	152.5	154.1	154.5	157.9
Percent Change	3.5	1.4	0.7	0.0	2.3	-1.4	-3.0	-1.9	1.1	0.2	2.2
February	151.5	150.8	151.3	151.0	151.2	150.5	155.4	150.7	151.0	152.3	157.0
Percent Change	3.0	-1.8	1.2	-0.8	0.7	-2.0	-3.0	-3.0	0.2	0.9	3.0
<b>Housing Permits</b>											
May	38.838	45.504	43.573	43.145	39.530	38.437	38.345	40.200	41.171	39.487	38.653
Percent Change	-26.6	88.4	-15.9	-3.9	-29.5	-10.6	-1.7	4.8	2.4	-4.1	-2.1
February	41.373	48.124	39.899	39.001	38.863	39.557	38.345	42.593	39.330	40.333	39.488
Percent Change	-23.5	83.1	-52.8	-8.7	-1.4	7.3	-1.7	11.1	-7.7	2.6	-2.1

Advisor's Name: \_\_\_\_\_

**Forecast Worksheet**  
**March 3, 2002**

	2003:Q2	2003	2004	Average 2005:1,2
<b><u>U.S.</u></b>				
<b>Real GDP, %Ch</b>				
Baseline	1.6	2.3	4.2	3.0
Your Opinion	_____	_____	_____	_____
<b>Implicit Price Deflator, % Ch</b>				
Baseline	1.4	1.9	1.6	1.8
Your Opinion	_____	_____	_____	_____
<b>Mortgage Rate, Percent</b>				
Baseline	5.8	5.9	6.5	6.9
Your Opinion	_____	_____	_____	_____
<b><u>Washington State</u></b>				
<b>Real Personal Income, % Ch</b>				
Baseline	3.6	1.3	2.5	2.9
Your Opinion	_____	_____	_____	_____
<b>Wage and Salary Employment, % Ch</b>				
Baseline	-1.4	-0.3	1.4	2.0
Your Opinion	_____	_____	_____	_____
<b>Manufacturing Employment, % Ch</b>				
Baseline	-5.2	-5.6	-1.8	2.3
Your Opinion	_____	_____	_____	_____
<b>Construction Employment, % Ch</b>				
Baseline	0.0	1.1	0.2	2.5
Your Opinion	_____	_____	_____	_____
<b>Housing Permits (Thousands)</b>				
Baseline	43.1	41.2	39.5	38.3
Your Opinion	_____	_____	_____	_____
<b>Washington Average Annual Wage, % Ch</b>				
Baseline	7.4	2.6	2.8	3.0
Your Opinion	_____	_____	_____	_____